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**UNITED STATES DISTRICT COURT FOR THE DISTRICT OF UTAH
CENTRAL DIVISION**

**SECURITIES AND EXCHANGE
COMMISSION,**

Plaintiffs,

v.

**ART INTELLECT, INC., a Utah
corporation, d/b/a MASON HILL and
VIRTUAL MG, PATRICK MERRILL
BRODY, LAURA A. ROSER, and
GREGORY D. WOOD,**

Defendants.

**MEMORANDUM IN SUPPORT OF
RECEIVER'S MOTION FOR ORDER
APPROVING SETTLEMENT
AGREEMENT AND TRANSFER AND
ABANDONMENT OF PROPERTIES**

Case No. 2:11-cv-00357 TC

Honorable Tena Campbell

R. Wayne Klein, the Court-Appointed Receiver (the "Receiver") of Art Intellect, Inc. d/b/a Mason Hill and VirtualMG submits this memorandum in support of his motion for approval of a settlement agreement reached between the Receiver and the Kenneth J. Hills and Marci Hills Retirement Profit Sharing Plan ("Hills"). A copy of the proposed settlement agreement is attached as Exhibit A to the Motion.

BACKGROUND

The Receiver has determined that the Receivership Estate owns five real estate properties in Lee County, Florida. All five of these properties are subject to liens related to loans made to Art Intellect by three lenders. The properties are:

1. 1138 SW 1st Terrace, Cape Coral, FL. This home is in the name of Art Intellect. It was purchased December 30, 2010 for \$62,400.00. It is subject to a \$55,000.00 mortgage held by Hills.
2. 5217 29th Street SW, Lehigh Acres, FL. This home is in the name of Art Intellect. It was purchased April 4, 2011 for \$71,000.00. The home is subject to a \$68,000.00 mortgage held by Hills.
3. 112/114 Pullman Street, Lehigh Acres, FL. This home is in the name of Mason Hill Properties, LLC. It was purchased on December 30, 2010 for \$62,400.00. It is subject to a \$60,000.00 mortgage held by Hills.
4. 3963/3965 20th Street W, Lehigh Acres, FL. This home is in the name of Art Intellect. It was purchased September 20, 2010 for \$71,500.00. The home is subject to two mortgages. The first mortgage is for \$51,000.00 held by Hills; the second mortgage is for \$65,000.00, held by Robert Lee.
5. 340/342 Rogen Street, Lehigh Acres, FL. This home was purchased on May 27, 2010 for \$50,100.00. It is subject to a \$40,000.00 first mortgage held by Michael Seybold and a second mortgage, in the amount of \$51,000.00, in favor of Hills.

Collectively, the seven mortgages are for an aggregate amount significantly greater than the value of the five properties.¹ For three of the homes, Pullman Street, 20th Street, and Rogen Street, the mortgages on the homes are greater than the net value of the homes. The Receiver believes that only the 1st Terrace and 29th Street properties have net equity.²

Because of the low equity value, the Receiver has been constrained in the options he might pursue in selling or otherwise recovering value from these properties. The Receiver has

¹ The total purchase price for these five properties was \$317,400.00. The seven mortgages total \$390,000.00.

² While the 29th Street property appears to have a small amount of equity, that equity is likely to disappear after closing costs, real estate fees, and expenses of the Receiver.

asserted claims against Hills, alleging that the amount he is due on his mortgages should be reduced. Hills has provided substantial information to the Receiver and the Receiver and Hills have engaged in extensive negotiations over an extended period of time. Those discussions have led to a settlement agreement with the terms described below.

SETTLEMENT AGREEMENT

Under the settlement agreement, the Receiver will release his claims to four of the five properties, Hills will pay \$25,000.00 to the Receivership Estate, and thereafter the Receiver will release his mortgage on the fifth property. Specifically,

1. The Receiver will sign deeds in lieu of foreclosure in favor of Hills for three properties: Pullman Street, 1st Terrace, and 29th Street.
2. The Receiver will abandon any claim to or interest in the 20th Street property, permitting Hills to initiate foreclosure actions against this property.
3. Hills will pay to the Receiver \$25,000.00 from the proceeds of the first sale of one of these properties, but no later than 60 days after the date of approval of this settlement agreement by the Court.
4. Hills will release his mortgage on the Rogen Street property and any claims to the promissory note associated with that property.
5. The Receiver will pay to the property manager selected by Hills the amounts paid by tenants as security deposits relating to the first three properties which were frozen by the Court on April 18, 2011. Net rental income earned by the Receivership Entities on the Pullman, 1st Terrace, and 29th Street properties will be paid to Hills as of August 1, 2011. Net rental income earned by the Receivership Entities on the 29th Street property will be allocated to Hills

as of July 1, 2011 and will be paid to Hills when Hills initiates legal proceedings to foreclose on the 29th Street property.

6. Both the Receiver and Hills agree to release all claims they might have against each other relating to these matters or any future claims.

7. The terms of this settlement agreement are subject to approval by the Court. If the Court declines to approve this agreement, the agreement will be rescinded.

TERMS OF THE REQUESTED COURT APPROVAL

The Receiver requests that the Court enter an order containing the following provisions:

1. Authorizing the Receiver to sign deeds in lieu of foreclosure for the Pullman, 1st Terrace, and 29th Street properties;
2. Authorizing the Receiver to abandon any claim to, or interest in, the 20th Street property and declaring that the 20th Street property is no longer deemed property of the Receivership Estate;
3. Releasing the four properties from the coverage of the asset freeze imposed by the Court on April 18, 2011; and
4. Otherwise approving the terms of the proposed settlement agreement and permitting the Receiver to move forward to implement its terms.

ANALYSIS

Paragraph 40 of the Order Appointing Receiver provides: "Upon further Order of this Court, pursuant to such procedures as may be required by this Court and additional authority such as 28 U.S.C. §§ 2001 and 2004, the Receiver will be authorized to sell, and transfer clear title to, all real property in the Receivership Estates."

Initially, it must be remembered that the Court is the one having “exclusive jurisdiction and possession of the assets” of Art Intellect, Brody, and Roser. Order at ¶1. After taking control of those assets, the court appointed Receiver for the Receivership Estate. Order at ¶2. The Court directed the Receiver to “determine the nature, location and value of all property interests” (Order at ¶8A), “take custody, control and possession of all Receivership Property” (Order at ¶8B), “use Receivership Property for the benefit of the Receivership Estates” (Order at ¶8D), “take immediate possession of all real property of the Receivership Defendants” (Order at ¶20), and “take all necessary and reasonable actions to cause the sale or lease of all real property in the Receivership Estates . . . on terms and in the manner the Receiver deems most beneficial to the Receivership Estate [subject to Court approval]” (Order at ¶39).

While the transfer of property proposed by this settlement agreement is not a sale or lease of the property, it is a disposition that results in substantial value for the Receivership Estate. This transfer eliminates \$234,000.00 in liabilities of the Receivership Estate and will result in the payment of \$25,000.00 to the Receivership Estate. The settlement agreement has the added advantage of freeing the Receiver and the Receivership Estate of the need to continue spending time and Receivership monies to protect and maintain these properties.

Moreover, this negotiated settlement eliminates the cost of litigating against the Hills in an effort to recover value from these properties and eliminates the risk of litigation. While the Receiver believes that he had a valid basis for asserting claims against the Hills, the Receiver’s position was not certain and the Court might not have agreed with his legal theory. The avoidance of risk and litigation costs is especially important in light of the relatively small value of equity in these properties. While the amount being recovered is relatively small, that is a

result of the actions of Defendants in mortgaging these properties for amounts higher than their value, thus reducing these properties as potential sources of recovery for victims of the Ponzi scheme.

The Securities and Exchange Commission has advised the Receiver that the Commission does not oppose this settlement. The Receiver is not aware of any others who might object to this settlement.

The Court Ordered and authorized the Receiver that “Upon further Order of the Court, pursuant to such procedures as may be required by this Court and additional authority such as 28 U.S. §§ 2001 and 2004, the Receiver will be authorized to sell, and transfer clear title to, all real property in the Receivership Estates.” Order ¶40. Pursuant to 28 U.S.C. § 2001, property in possession of the receiver is typically sold “at public sale.” However, section 2001 (b) allows “the court may order the sale of such realty . . . at private sale for cash or other consideration and upon such terms and conditions as the court approves, if it finds that the best interests of the estate will be conserved thereby.” 28 U.S.C. § 2001(b). This section typically requires as well that appraisals be had and other notice be provided. However, the Court, as discussed herein, can order the private sale or order other relief “if it finds that the best interests of the estate will be conserved thereby.” *Id.*

This case justifies such a finding by the Court. First, these are not a “sale” under the statute, but instead the disposition of the property by deeds in lieu of foreclosure and abandonment. Ultimately, the properties are going to the mortgagor. Second, the liens in place are for virtually the entire value of the properties. As discussed above, there is not enough net equity to justify spending the Estate’s money to pay for three independent appraisals for each of

the properties, or to engage agents and pay commissions. Furthermore, the estate needs to avoid the additional expenses associated with the maintenance of the properties. Finally, because the purchase of the properties was so recent, the Receiver is confident of the properties' current value. Moreover, comparisons to comparable properties in the area demonstrate that the prices paid and the current values remain similar. In short no formal appraisals, that would cost thousands of dollars, are necessary given the circumstances relating to these properties. As such, the Court should approve the disposition of the properties as contemplated in the proposed settlement agreement since this would best preserve the Estate.

CONCLUSION

The Receiver asks the Court to approve the terms of the proposed settlement agreement with the Hills as being in the best interests of the Receivership Estate and enter an order similar to the attached proposed Order.

DATED this 20th day of July 2011.

CLYDE SNOW & SESSIONS

/s/ Jennifer A. James

Jennifer A. James

Walter A. Romney, Jr.

Attorneys for Court-Appointed

Receiver R. Wayne Klein

CERTIFICATE OF SERVICE

IT IS HEREBY CERTIFIED that service of the above **MEMORANDUM IN SUPPORT OF RECEIVER'S MOTION FOR ORDER APPROVING SETTLEMENT AGREEMENT AND TRANSFER AND ABANDONMENT OF PROPERTIES** was served via the CM/ECF system on this 20th day of July 2011 on the following:

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Court-Appointed Receiver

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